Testimony

To: House of Representatives Judiciary Committee
Representative Lance Kinzer, Chair

From: Allie Devine, Devine & Donley, LLC on behalf of livestock producer clients, and the National Cattlemen's Beef Association

Date: May 11, 2012

Re: HB 2797

Mr. Chairman, Members of the Committee, thank you for holding this hearing on HB 2797. We support the bill. It is necessary to avert the chaos that will likely result from the ruling in *O'Brien v. Leegin*, which others have or will outline. My comments today will focus on the problems created for livestock producers and processors by this ruling.

In summary, the regulation of marketing of livestock and meat products is governed by the federal Packers and Stockyards Act (PSA). The federal courts have consistently incorporated the rule of reason analysis in determining anti competitive claims under the PSA. The *O'Brien* decision, removing the rule of reason analysis from interpretations of Kansas anti trust law, places a huge secondary regulatory burden on the formation and use of contracts. The Kansas Supreme Court noted that KSA 50-101 *et. seq.* is an "undeveloped area of law" and this ruling provides little guidance to industry as to what is or is not acceptable practice. HB 2797 inserts the well-known principles and analysis of the "rule of reason" into Kansas law thus assuring consistent interpretation of the state and federal laws and provides certainty to industries operating in both jurisdictions.

Background:

There are four key sectors of the beef supply chain: cow calf production; cattle feeding; packing/processing; and retail sales. Like all other industries, there are a variety of factors that effect product pricing. In beef some of those factors are demand, production (supply and quality), trade, interest rates/ availability of capital, and governmental policies.

Nearly 30 years ago, the beef industry was in decline as other protein sources, (pork and poultry) gained market share. The beef industry was selling a "generic commodity" and consumers were not buying. Consumers had shifted to pork and poultry where price and product consistency was more desirable. These industries had "vertically integrated" to control supply, quality, and price. To increase demand, the beef industry focused on improving genetics, removing inefficiencies in

production, and coordinating within industry segments to improve quantity, quality, and consistency.

The industry has developed a variety of alternative marketing arrangements (AMAs) or marketing agreements between producers, processors, and some retailers. Producers have sought these agreements. These marketing agreements (contracts) are critical tools to improve efficiencies in the supply chain; improve demand; reduce transaction costs, and provide some risk management. Marketing agreements allow higher value and value added beef products to be sold to consumers that value and demand such products. Reduced costs and improved demand has resulted in higher beef prices, higher fed cattle prices, and higher feeder cattle and calf prices and more profits to producers. In short, marketing agreements have provided the industry with a method of sending marketing signals up and down the supply chain and provided rewards to those who respond to the market demands and have provided consumers with a product they desire.

Regulatory oversight of the market place:

The use of marketing agreements has been just one of several structural changes taking place in agriculture. As structural change has taken place so has governmental oversight and antitrust litigation. Traditionally, livestock has been regulated by the federal government through the Packers and Stockyards Act (PSA) which has its roots in the Sherman antitrust act.

Over the past 15 years, eight federal Courts of Appeals have reviewed the PSA and have consistently ruled that provisions of PSA are violated only if the practice in question has had, or is likely to have an adverse effect on competition. [i] In 2010, the United States Department of Agriculture Grain Inspection Packers and Stockyards Administration (GIPSA) proposed regulations further seeking to "define" what was "competitive injury" (note difference in terminology to "injury to competition") The rule of reason, has been a critical tenet of law governing livestock transactions. Below is an excerpt from NCBA comments to USDA outlining the history of antitrust policy, the PSA, the importance of the rule of reason analysis and its impact on livestock transactions.

"The Supreme Court has made it clear that antitrust law protects competition, not competitors. Thus, the "competitive injury" with which the Court (and antitrust law) is concerned is injury to the overall functioning of markets, not some form of disadvantage to particular market participants. Accordingly, in determining whether an alleged restraint of trade causes this kind of "competitive injury," a court applying antitrust's basic Rule of Reason typically analyzes three issues. First, what are the relevant product and geographic markets in which the restraint's effect on competition should be assessed? Second, does the defendant have a high share of the relevant market, and would the restraint enhance that market power? Third, do the restraint's adverse effects on competition outweigh the offsetting competitive benefits of the restraint, such as facilitating risk management, creating operating efficiencies, enhancing or controlling quality, or increasing consumer choice? Only if the adverse effects predominate is the

restraint unlawful. ***This assessment calls for a very careful and discerning inquiry because, without a proper balancing of competitive interests, antitrust law could come to stifle the innovation and efficiency that Congress intended it to promote. (emphasis added)*** *See, e.g., Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977); Leegin Creative Leather Prods. v. PSKS, Inc., 551 U.S. 877 (2007)." See* Farm Bill Comments of the National Cattlemen's Beef Association (NCBA) on proposed Farm Bill Regulations, 75 Fed. Reg. 35338-35354 (June 22, 2012).

USDA withdrew a majority of the proposed regulation after public comment.

The bolded language above illustrates the importance of the rule of reason analysis. The practical problem created by the O'Brien decision is that the court has eliminated the analysis of balancing competitive interests. As the Supreme Court has warned, without a proper balancing of competitive interests, antitrust law could come to stifle innovation and efficiency.

As a practical matter, producers and processors are negotiating contractual relationships every day. What relationships, written or otherwise are lawful under the Kansas law? How do industries seek a profit to remain in business while meeting the requirements of KSA 50-112? The law is antiquated. It worked for an 1800's century generic commodity marketplace but not in a 21st century environment with thousands of products to meet consumer demands.

We urge passage of HB 2797 to immediately calm the situation and ask the legislature to review this issue extensively over the summer.

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[i] See *Terry v. Tyson Farms, Inc.,* 604 F. 3d 272 (6th Cir. 2010),*Wheeler v. Pilgrim's Pride Corp.*, 591 F.3d 355 (5th Cir. 2009) (en banc); *Been v. O.K. Indus., Inc.*, 495 F.3d 1217, 1230 (10th Cir.2007); *Pickett v. Tyson Fresh Meats, Inc.*, 420 F.3d 1272, 1280 (11th Cir.2005), *cert. denied,* 547 U.S. 1040, 126 S.Ct. 1619, 164 L.Ed.2d 333 (2006); *London v. Fieldale Farms Corp.*, 410 F.3d 1295, 1303 (11th Cir.2005), *cert. denied,* 546 U.S. 1034, 126 S.Ct. 752, 163 L.Ed.2d 574 (2005); *IBP, Inc. v. Glickman,* 187 F.3d 974, 977 (8th Cir.1999); *Philson v. Goldsboro Milling Co.*, Nos. 96-2542, 96-2631, 164 F.3d 625, 1998 WL 709324, at *4-5 (4th Cir. Oct.5, 1998) (unpublished table decision); *Jackson v. Swift Eckrich, Inc.*, 53 F.3d 1452, 1458 (8th Cir. 1995); *Farrow v. United States Dep't of Agric.*, 760 F.2d 211, 215 (8th Cir.1985); *De Jong Packing Co. v. United States Dep't of Agric.*, 618 F.2d 1329, 1336-37 (9th Cir. 1980), *cert. denied,* 449 U.S. 1061, 101 S.Ct. 783, 66 L.Ed.2d 603 (1980); and *Pac. Trading Co. v. Wilson & Co.*, 547 F.2d 367, 369-70 (7th Cir.1976).